91-1464

(1)

No.

Supreme Court, U.S.
FILED
MAR 3 1992
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

WILSON S. PALMER,
Petitioner,

vs.

TED R. LEVY,
Respondent.

PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

RICHARD MICHAEL MONEYMAKER
Counsel of Record
VINCENT BRUCE MONEYMAKER

Law Firm of
RICHARD M. MONEYMAKER

700 South Flower Street
Suite 2102
Los Angeles, California 90017
(213) 622-1088

Attorneys for Petitioner
WILSON S. PALMER

Lawyers Brief Service • Appellate Brief Printers • (213) 613-1013 • (714) 720-1510

QUESTION PRESENTED

1. Did the Ninth Circuit err in holding that punitive damages assessed as a result of a fraudulent act are dischargeable under Bankruptcy Code Section 523(a); or did the Eighth and Eleventh Circuits correctly hold, pursuant to section 523(a)'s plain language, that "any debt", including one for punitive damages, is non-dischargeable as long as the debt arises from one of the acts or circumstances described in section 523(a)?

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
TABLE OF AUTHORITIES	iv
OPINIONS BELOW	1
JURISDICTION	2
STATUTE INVOLVED	3
STATEMENT OF THE CASE.	4
REASONS FOR GRANTING THE WRIT. . . .	10
I. THE NINTH CIRCUIT'S DECISION IN PALMER v. LEVY DIRECTLY CONFLICTS WITH DECISIONS OF TWO OTHER CIRCUIT COURTS. . .	12
II. THE NINTH CIRCUIT'S PALMER DECISION DIRECTLY CONFLICTS WITH THE PLAIN MEANING OF THE BANKRUPTCY CODE'S NONDISCHARGEABILITY SECTION .	14
III. THE LEGISLATIVE HISTORY ACCOMPANYING THE BANKRUPTCY CODE'S NONDISCHARGEABILITY SECTION DOES NOT SUPPORT THE NINTH CIRCUIT'S INTERPRETATION OF THAT SECTION	17
IV. THE PALMER DECISION CONFLICTS WITH THE WELL ESTABLISHED POLICY OF EXTENDING THE DISCHARGE PRIVILEGE TO ONLY THE 'HONEST, BUT UNFORTUNATE DEBTOR.'.	20

TABLE OF CONTENTS - CONTINUED

Page

V. THE NINTH CIRCUIT'S PALMER DECISION INDIRECTLY CONFLICTS WITH THIS HONORABLE COURT'S DECISION IN GROGAN V. GARNER. 22

CONCLUSION 25

APPENDIX A

OPINION, UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT, FILED DECEMBER 6, 1991. . . . . A-1

APPENDIX B

MEMORANDUM DECISION, UNITED STATES BANKRUPTCY APPELLATE PANEL OF THE NINTH CIRCUIT, FILED MAY 25, 1990. . . . . B-1

APPENDIX C

JUDGMENT, UNITED STATES BANKRUPTCY COURT, CENTRAL DISTRICT OF CALIFORNIA, ENTERED JANUARY 27, 1987. . . . C-1

APPENDIX D

FINDINGS OF FACT AND CONCLUSIONS OF LAW ENTERED JANUARY 27, 1987. . . . . D-1

TABLE OF AUTHORITIES

UNITED STATES SUPREME COURT — **Page**

Grogan v. Garner, ___ U.S. ___, 111 S. Ct. 654, ___ L. Ed. 2d ___ (1991) 12, 23, 25

Local Loan Co. v. Hunt, 292 U.S. 234, 54 S. Ct. 695, 78 L. Ed. 1230, (1934) 21

United States v. Ron Pair Enter., Inc., 489 U.S. 235, 109 S. Ct. 1026, 103 L. Ed. 2d 290 (1989) . . 16

Williams v. United States Fidelity & Guar. Co., 236 U.S. 549, 35 S. Ct. 289, 59 L. Ed. 713, (1915). 21

CIRCUIT COURT OF APPEALS — **Page**

Birmingham Trust Nat'l Bank v. Case, 755 F.2d 1474 (11th Cir. 1985) . . 12, 13-14, 22

Johnson v. Miera (In re Miera), 926 F.2d 741 (8th Cir. 1991) . . . 12, 13-14, 16

Northern Trust Co. v. Garman (In re Garman), 643 F.2d 1252, 1257 (7th Cir. 1980), cert. denied, 450 U.S. 910, 101 S. Ct. 1347, 67 L. Ed. 2d 333 (1981). 21-22

BANKRUPTCY APPELLATE PANELS

Ellwanger v. McBroom (In re Ellwanger), 105 Bankr. 551, 555 (Bankr. 9th Cir. 1989) 14, 16

TABLE OF AUTHORITIES - CONTINUED

UNITED STATES STATUTES — **Page**

11 U.S.C. § 157(b)(2)(I) 5
11 U.S.C. § 158(b) 6
11 U.S.C. § 158(d) 6
11 U.S.C. § 523(a) . 12-15, 18-21, 25-26
11 U.S.C. § 523(a)(2). 3-4, 8-10, 16, 24
11 U.S.C. § 1254(1). 3

LEGISLATIVE MATERIALS

130 Cong. Rec. H6087-6088
(daily ed. June 19, 1984). 20
130 Cong. Rec. S7617-7625
(daily ed. June 19, 1984). 20
130 Cong. Rec. H7471-7500
(daily ed. June 29, 1984). 20
130 Cong. Rec. S8887-8900
(daily ed. June 29, 1984). 20

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1991

No.____

WILSON S. PALMER,
Petitioner,

v.

TED R. LEVY,
Respondent,

Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

---

PETITION FOR WRIT OF CERTIORARI

The Petitioner respectfully prays that a Writ of Certiorari issue to review a decision of the United States Court of Appeals for the Ninth Circuit.

OPINIONS BELOW

The Opinion of the United States Court of Appeals for the Ninth Circuit is reprinted as Appendix A herein. At this

time, the Petitioner does not have the actual Federal Reporter citation for the Opinion. The slip opinion citation is Palmer v. Levy (In re Levy), No. 95-55851 (9th Cir. Dec. 6, 1991).

The Memorandum Decision of the United States Bankruptcy Appellate Panel of the Ninth Circuit, which was not published, is reprinted as Appendix B herein.

The Judgment of the United States Bankruptcy Court, Central District of California, which also was not published, is reprinted as Appendix C herein.

The Findings of Fact and Conclusions of Law of the United States Bankruptcy Court, Central District of California, is reprinted as Appendix D herein.

JURISDICTION

The Opinion of the Court of Appeals for the Ninth Circuit was filed on

December 6, 1991, affirming the Memorandum Decision of the United States Bankruptcy Appellate Panel of the Ninth Circuit, which, in turn, affirmed the Judgment of the United States Bankruptcy Court, Central District of California, in favor of the Respondent. This Court's jurisdiction is invoked pursuant to 28 U.S.C. Section 1254(1).

STATUTE INVOLVED

This case involves the question of whether punitive damages are non-dischargeable under Section 523(a) of the Bankruptcy Code. Section 523(a) provides in pertinent part that:

> (a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from <u>any debt</u> -
>
> (2) for money, property, services, or an extension,

renewal, or refinancing of credit, to the extent obtained, by -

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition

. . . .

(emphasis added).

STATEMENT OF THE CASE

This case involves the issue of whether any portion of a debt which flows from an act or circumstance described in the Non-Dischargeability Section of the Bankruptcy Code can be declared dischargeable. The courts of appeals of three circuits have divided on this issue, with the Ninth Circuit holding that the punitive damages portion of a state court judgment based

upon fraud can be discharged in bankruptcy.

The hearing of this case is of crucial importance because if the Ninth Circuit's minority ruling is allowed to stand, it will result in hundreds, if not thousands, of future unscrupulous debtors being able to discharge that portion of the fraud judgments rendered against them for which they have been found most culpable.

BASIS FOR FEDERAL JURISDICTION

The jurisdiction of the United States Bankruptcy Court for the Central District of California to consider the issue of the non-dischargeability of Palmer's judgment against Levy is provided by 28 U.S.C. Section 157(b)(2)(I) which grants bankruptcy courts jurisdiction to hear core proceedings involving the determination

of the dischargeability of particular debts.

The jurisdiction of the United States Bankruptcy Appellate Panel of the Ninth Circuit to hear Palmer's timely appeal from the bankruptcy court's final judgment against Palmer is provided by 28 U.S.C. Section 158(b) which grants bankruptcy appellate panels jurisdiction to hear appeals from final judgments of bankruptcy courts.

The jurisdiction of the United States Court of Appeals for the Ninth Circuit to hear Palmer's timely appeal from the Ninth Circuit's Bankruptcy Appellate Panel is provided by 28 U.S.C. Section 158(d) which grants the circuit courts of appeals jurisdiction to hear appeals from final judgments of bankruptcy appellate panels entered pursuant to 28 U.S.C. Section 158(b).

STATEMENT OF FACTS

The facts in this case are undisputed. The Respondent, Ted R. Levy, hired the Petitioner, Wilson S. Palmer, as a real estate salesman upon a promise to pay him both commissions and a percentage of profits made from business which Palmer generated for Levy.

Levy reneged on his promise to Palmer under circumstances which caused Palmer to sue Levy for fraud in a California state court. After a lengthy jury trial, Palmer obtained a judgment against Levy on the fraud count for $45,612.39 in compensatory damages, plus $250,000.00 in punitive damages.

Levy responded by filing a voluntary petition for relief under Chapter 7 of the Bankruptcy Code. Palmer then filed a timely complaint in the bankruptcy court to determine the non-

dischargeability of Levy's debt.

On January 5, 1987, the bankruptcy judge held a mini-trial on the issue of non-dischargeability. The state court transcript was offered into evidence and portions were read into the record. Palmer's state court lawyer testified, as did Palmer.

At the end of the trial, the bankruptcy judge found that Palmer's state court judgment against Levy was based upon fraud and false pretenses within the meaning of Section 523(a)(2) of the Bankruptcy Code and, thus, the judgment was non-dischargeable to the extent of $45,612.39.

However, the bankruptcy judge, in a claimed exercise of his discretion, declined to hold that the $250,000.00 punitive damage portion of the state court judgment was non-dischargeable.

As a result, the bankruptcy judge, on January 27, 1987, entered his judgment discharging Levy from legal responsibility for the $250,000.00 punitive damage portion of the state court judgment.

Palmer timely filed his Notice of Appeal from the bankruptcy court judgment on February 3, 1987. On May 25, 1990, the United States Bankruptcy Appellate Panel of the Ninth Circuit filed its unpublished Memorandum Decision affirming the decision of the bankruptcy court that punitive damages are dischargeable under section 523(a)(2).

On June 21, 1990, Palmer timely filed his Notice of Appeal to the United States Court of Appeals for the Ninth Circuit from the unpublished Memorandum Decision of the bankruptcy appellate

panel. On December 6, 1991, the Ninth Circuit filed its published Opinion holding that punitive damages assessed against them as a result of an act of fraud are dischargeable under section 523(a)(2). In response, Palmer timely filed this Petition for Writ of Certiorari.

REASONS FOR GRANTING THE WRIT

In this case, the Ninth Circuit has decided, in a published opinion, that admittedly dishonest debtors may discharge punitive damages assessed as a result of their fraudulent acts. This decision must not be allowed to stand for the following reasons.

First, the Ninth Circuit's decision creates a direct conflict with decisions in the Eighth and Eleventh Circuits. In so doing, the Ninth Circuit's decision allows debtors who have fraud judgments

rendered against them to either fortuitously benefit from living within the Ninth Circuit's jurisdiction, or, more disturbingly, to actively forum shop their bankruptcies so as to take advantage of the Ninth Circuit's decision.

Second, the Ninth Circuit's decision conflicts with the plain meaning of the Bankruptcy Code's Nondischargeability Section.

Third, the legislative history accompanying the Bankruptcy Code's Nondischargeability Section does not support the Ninth Circuit's interpretation of that Section.

Fourth, the Ninth Circuit's decision conflicts with the well established policy of extending the discharge privilege to only the 'honest, but unfortunate debtor.'

Fifth, the Ninth Circuit's decision indirectly conflicts with this Court's decision in Grogan v. Garner.

I. THE NINTH CIRCUIT'S DECISION IN PALMER v. LEVY DIRECTLY CONFLICTS WITH DECISIONS OF TWO OTHER CIRCUIT COURTS.

In Johnson v. Miera (In re Miera), 926 F.2d 741 (8th Cir. 1991) and Birmingham Trust Nat'l Bank v. Case, 755 F.2d 1474 (11th Cir. 1985), the Eighth and Eleventh Circuits both ruled that the entire portion of a debt is nondischargeable as long as the debt arises from one of the acts or circumstances described in the Bankruptcy Code's Nondischargeability Section.

In so ruling, both Circuits found the opening language of section 523(a), which states that an individual debtor is not discharged from "any debt"

incurred as a result of an act or circumstance described in section 523(a), to be determinative of the issue. (emphasis added).

Specifically, the Eleventh Circuit stated in Birmingham that "the plain language of the statute suggests that dischargeability is an 'all or nothing' proposition." Birmingham, 755 F.2d at 1477 (emphasis in original).

Likewise, in Johnson, the Eighth Circuit found section 523(a)'s "any debt" language to be controlling with regard to the issue of whether punitive damages are nondischargeable. Johnson, 926 F.2d at 745 (emphasis in original).

In contrast, the Ninth Circuit, in its Palmer decision, completely ignored the "any debt" language found in section 523(a). Instead, the Ninth Circuit ruled that punitive damages assessed as

a result of fraud are dischargeable because such damages do not represent a debt "'obtained by actual fraud.'" Palmer, No. 90-55851, slip op at 15474 (9th Cir. Dec. 6, 1991) (citing Ellwanger v. McBroom (In re Ellwanger), 105 Bankr. 551, 555 (Bankr. 9th Cir. 1989)).

Accordingly, because the Ninth Circuit's Palmer ruling is in direct conflict with both the Eighth Circuit's Johnson ruling and the Eleventh Circuit's Birmingham ruling, and because this conflict will inevitably result in forum shopping on the part of dishonest debtors who seek to discharge sizable punitive damage awards, certiorari should be granted in order to resolve the circuit conflict presented in this case.

II. THE NINTH CIRCUIT'S PALMER DECISION DIRECTLY CONFLICTS WITH THE PLAIN MEANING OF THE BANKRUPTCY CODE'S NONDISCHARGEABILITY SECTION.

Section 523(a) of the Bankruptcy Code provides that

> (a) A discharge under . . . this title does not discharge an individual debtor from any debt -
>
> (2) for money, property, services, or an extension . . . of credit, to the extent obtained, by -
>
> (A) false pretenses, a false representation, or actual fraud . . . .

(emphasis added).

In its Palmer decision, the Ninth Circuit chose to ignore the plain meaning of the "any debt" language found in section 523(a). Instead, the Ninth

Circuit focused on the "to the extent obtained, by" language found in section 523(a)(2), and held, on that basis, that the "phrase [was] meant to limit the nondischargeable debt to the amount 'obtained by actual fraud.'" Palmer, No. 90-55851, slip op. at 15474 (citing Ellwanger, 105 Bankr. at 555) (further citation omitted).

In so holding, the Ninth Circuit violated the basic rule of statutory construction, which is to interpret a statute according to its plain meaning. See United States v. Ron Pair Enter., Inc., 489 U.S. 235, 109 S. Ct. 1026, 103 L. Ed. 2d 290 (1989).

In this case, the "to the extent obtained, by" language contained in section 523(a) is plainly directed "at the nature of the conduct which [gave] rise to the [nondischargeable] debt,

rather than to the nature of the debt." Johnson, 926 F.2d at 745.

As a result, since Palmer's judgment against Levy arose from services Levy obtained by actual fraud, Palmer's entire debt against Levy, including the punitive damages portion, should have been declared nondischargeable.

Accordingly, because the Ninth Circuit misinterprets the plain meaning of section 523(a) in its Palmer decision, certiorari should be granted in order to correct the Ninth Circuit's misinterpretation of the Bankruptcy Code.

III. THE LEGISLATIVE HISTORY ACCOMPANYING THE BANKRUPTCY CODE'S NONDISCHARGEABILITY SECTION DOES NOT SUPPORT THE NINTH CIRCUIT'S INTERPRETATION OF THAT SECTION.

In 1984, Congress amended section

523(a). Formerly, section 523(a) read as follows:

> (a) A discharge under . . . this title does not discharge an individual debtor from any debt -
>
> (2) for obtaining money, property, services, or an extension, renewal, or refinance of credit, by -
>
> (A) false pretenses, a false representation, or actual fraud . . . .

(subsequent deletions emphasized). After the amendment, section 523(a) read as follows:

> (a) A discharge under . . . this title does not discharge an individual debtor from any debt -
>
> (2) for money, property, services, or an extension, renewal, or refinancing of

credit, to the extent obtained, by -

(A) false pretenses, a false representation, or actual fraud . . . .

(additions emphasized).

In its Palmer decision, the Ninth Circuit stated that the 1984 amendment was "meant to limit the nondischargeable debt to the amount 'obtained by actual fraud.'" Palmer, No. 90-55851, slip op. at 15474. Notwithstanding this statement, the Ninth Circuit fails to reference any legislative history which would lead the Ninth Circuit to such a conclusion.

The reason for this is clear, the Ninth Circuit fails to include such a reference because there is no legislative history which states, or even implies, that Congress ever

intended to prevent punitive damage awards from being declared nondischargeable.

Clearly, if Congress had intended its 1984 amendment to have such a drastic effect on nondischargeability actions, Congress would have made some mention of its intended change in the law. However, as a review of the legislative history indicates, Congress made no mention of any change in the law regarding the nondischargeability of punitive damages. See 130 Cong. Rec. H6087-6088 (daily ed. June 19, 1984); 130 Cong. Rec. S7617-7625 (daily ed. June 19, 1984); 130 Cong. Rec. H7471-7500 (daily ed. June 29, 1984); 130 Cong. Rec. S8887-8900 (daily ed. June 29, 1984).

Accordingly, because the legislative history does not support the Ninth

Circuit's interpretation of section 523(a), this presents one further reason for why certiorari should be granted in this case.

IV. THE PALMER DECISION CONFLICTS WITH THE WELL ESTABLISHED POLICY OF EXTENDING THE DISCHARGE PRIVILEGE TO ONLY THE 'HONEST, BUT UNFORTUNATE DEBTOR.'

It is well established that Congress enacted the discharge privilege to provide only the 'honest, but unfortunate debtor' with a fresh start. See Williams v. United States Fidelity & Guar. Co., 236 U.S. 549, 554, 35 S. Ct. 289, 291, 59 L. Ed. 713, 716 (1915); see also Local Loan Co. v. Hunt, 292 U.S. 234, 244, 54 S. Ct. 695, 700, 78 L. Ed. 1230, 1235 (1934); see also Northern Trust Co. v. Garman (In re Garman), 643 F.2d 1252, 1257 (7th Cir. 1980), cert.

denied, 450 U.S. 910, 101 S. Ct. 1347, 67 L. Ed. 2d 333 (1981).

It is also well established that Congress "by creating fraud exceptions to discharge . . . sought to discourage fraudulent conduct and ensure that relief intended for honest debtors [did] not inure to the benefit of dishonest ones." Birmingham, 755. F.2d at 1477 (citation omitted).

In this case, it is undisputed that Levy is a dishonest debtor who is trying to discharge a fraud-based debt. Notwithstanding this fact, the Ninth Circuit still allowed Levy to discharge the major portion of the fraud judgment held against him. Thus, not only did the Ninth Circuit allow Levy to discharge a dishonestly incurred debt, but the Ninth Circuit actually allowed Levy to discharge that portion of the

debt which was most associated with Levy's dishonesty.

This action defies logic and, thus, presents one more reason for why certiorari should be granted in this case.

V. THE NINTH CIRCUIT'S PALMER DECISION INDIRECTLY CONFLICTS WITH THIS HONORABLE COURT'S DECISION IN GROGAN V. GARNER.

This Honorable Court recently handed down a decision in Grogan v. Garner, ___ U.S. ___, 111 S. Ct. 654, ___ L. Ed. 2d ___ (1991), which lends further support to the contention of Palmer that the Ninth Circuit erred when it ruled the punitive damages portion of Palmer's judgment against Levy was dischargeable.

In Grogan, the debtor Garner defrauded the creditor Grogan. Grogan subsequently sued Garner and obtained a

judgment against him. Per the judgment, Grogan was awarded both actual and punitive damages.

Thereafter, Garner attempted to discharge the debt owed Grogan by filing a petition for relief under Chapter 11. In response, Grogan filed a nondischargeability complaint against Garner. Grogan based his complaint on section 523(a)(2).

In ruling on the complaint, both the bankruptcy court and the district court found that the entire judgment, including the punitive damages portion, should be declared nondischargeable. The United States Court of Appeals for the Eighth Circuit, however, disagreed, but only on the narrow ground that the bankruptcy court had applied an inappropriate standard of proof to its nondischargeability determination.

After granting certiorari, this Honorable Court reversed the Eighth Circuit ruling. The practical effect of this reversal was to endorse the line of authority which holds that punitive damages are nondischargeable when they are awarded on a claim which is itself nondischargeable.

Further support for the conclusion that this Honorable Court, in Grogan, intended to endorse the view that no distinction should be made between the nondischargeability of actual damages and punitive damages can be garnered from the Grogan Syllabus.

In the Syllabus, the statement is made that "all fraud claims [which] creditors have [successfully] reduced to judgment" are nondischargeable. Grogan, 111 S. Ct. at 656 (emphasis added).

Because this statement is not

qualified or limited in any manner, it can plainly be read to mean that all fraud damages are nondischargeable regardless of whether they are actual or punitive in nature.

Accordingly, because this Honorable Court has already indicated that, if given the chance, it would hold that punitive damages are nondischargeable under 523(a), certiorari should be granted in order to allow this Honorable Court to do just that.

CONCLUSION

WHEREFORE, Petitioner, Wilson S. Palmer, prays that a writ of certiorari issue from this Honorable Court to review the judgment of the United States Court of Appeals for the Ninth Circuit in Palmer v. Levy (In re Levy). In the event the petition is granted, Petitioner prays that the judgment of

the Ninth Circuit be reversed and that the cause be remanded with directions to reverse both the judgments of the United States Bankruptcy Appellate Panel of the Ninth Circuit and the United States Bankruptcy Court for the Central District of California.

Respectfully submitted,

Richard Michael Moneymaker
Counsel of Record
Vincent Bruce Moneymaker
Law Firm of Richard M. Moneymaker
700 South Flower Street, Suite 2102
Los Angeles, California 90017
(213) 622-1088
Attorneys for Petitioner,
Wilson S. Palmer

APPENDIX A

OPINION

FLETCHER, Circuit Judge:

In this case, we consider the scope of section 523(a)(2) of the Bankruptcy Code, which bars discharge of a debt for money or property obtained by fraud. At issue is whether that section excepts from discharge punitive damages as well as actual damages. Wilson Palmer appeals from the decision of the Bankruptcy Appellate Panel affirming the bankruptcy court's finding that the punitive damages portion of a judgment Palmer had obtained against Ted Levy, the debtor, was dischargeable. We affirm.

BACKGROUND

Levy was one of the principals of three corporations involved in real estate development and sales. These corporations hired Palmer as a salesman, promising to pay him both commissions and a percentage of profits from the business he brought in. The corporations breached the employment contract, and Palmer sued in California state court for fraud and misrepresentation. The jury awarded Palmer $53,538.94 in compensatory damages (of which $45,612.38 were damages for fraud and misrepresentation) and punitive damages of $250,000. Levy appealed this decision. While the appeal was pending he filed a Chapter 7 bankruptcy petition.

Palmer filed a complaint with the bankruptcy court seeking a determination that Levy's debt to him on the judgment against Levy was nondischargeable. The bankruptcy court held after a hearing that the $45,612.38 damages for fraud were nondischargeable. It also concluded, however, that it had discretion to discharge and did discharge the debt for the $250,000 punitive damages portion of the judgment.

Palmer appealed to the BAP, arguing that the bankruptcy court had erred in discharging the punitive damages portion of the debt. The BAP affirmed, holding that the section 523(a)(2) excepted from discharge only actual damages for fraud.[1]

STANDARD OF REVIEW

Palmer's appeal presents an issue of law. We review such issues de novo. *Romley v. Sun National Bank (In re Two "S" Corp.)*, 875 F.2d 240, 242 (9th Cir. 1989).

DISCUSSION

Section 523(a)(2)(A) provides, in relevant part:

> (a) A discharge under section 727 ... of this title does not discharge an individual debtor from any debt—
>
> > (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by—
> >
> > > (A) false pretenses, a false representation, or actual fraud ...

11 U.S.C. § 523 (a)(2)(A).

[1] The Ninth Circuit has not decided the issue of whether punitive damages are excepted from discharge under this section. The BAP, however, has resolved this question in *In re Ellwanger*. In that case, the BAP held that under section 523(a)(2), "a wholly private penalty cannot be the basis for a nondischargeability judgment." *Ellwanger v. McBroom (In re Ellwanger)*, 105 B.R. 551, 555 (Bankr. 9th Cir. 1989). Other

[1]Levy has not filed a brief or appeared in either Palmer's appeal to the BAP or this appeal.

bankruptcy courts addressing the issue have generally found that section 523(a)(2) does not bar discharge of punitive damages. *See, e.g., Larson v. Norris* (*In re Larson*), 79 B.R. 462 (Bankr. W.D.Mo. 1987); *Haile v. McDonald* (*In re McDonald*), 73 B.R. 877 (Bankr. N.D.Tex. 1987); *Jones v. Wilson* (*In re Wilson*), 72 B.R. 956 (Bankr. M.D.Fla. 1987); *McCullough v. Suter* (*In re Suter*), 59 B.R. 944 (Bankr. N.D.Ill. 1986).

Palmer argues that the BAP erred in distinguishing among the various subsections of section 523 on the issue of the discharge of punitive damages. He notes that courts have found that punitive damages are nondischargeable under section 523(a)(4), which bars discharge of debts "for fraud or defalcation while acting in a fiduciary capacity, embezzlement or larceny," 11 U.S.C. § 523(a)(4), and under section 523(a)(6), which bars discharge of debts "for willful and malicious injury by the debtor to another entity or to the property of another entity," 11 U.S.C. § 523(a)(6). *See, e.g., Klemens v. Wallace* (*In re Wallace*), 840 F.2d 762 (10th Cir. 1988) (holding, without discussion of the punitive damages issue, that judgment for embezzlement which included actual and punitive damages was nondischargeable); *Moraes v. Adams* (*In re Adams*), 761 F.2d 1422, 1428 (1985) (section 523(a)(6) bars discharge of both punitive and actual damages); *Brawer v. Gelman* (*In re Gelman*), 47 B.R. 735 (Bankr. S.D. Fla. 1985) (holding, without discussion of the punitive damages issue, that both actual and punitive portions of judgment for defalcation while acting in a fiduciary capacity were nondischargeable). Palmer argues that there is no basis in section 523 for such a distinction.

[2] We find, however, that an examination of both the language of section 523(a)(2) and the structure established in section 523 as a whole supports a conclusion that section 523(a)(2), unlike sections 523(a)(4) and 523(a)(6), does not bar discharge of punitive damages.

I. The Language of Section 523(a)(2)

In its decision in this case, the BAP looked to the language of section 523(a)(2) to support its holding on that section. In 1984, the subsection was amended to add the language "to the extent obtained by."[2] This phrase is meant to limit the nondischargeable debt to the amount "obtained by actual fraud." *Ellwanger*, 105 B.R. at 555; *In re Suter*, 59 B.R. at 946 ("[section] 523(a)(2)(A) precludes the dischargeability of a debt for money *only* to the extent the money was obtained by actual fraud"). Punitive damages, in contrast, do not represent losses to the victim of fraud or increases in the wealth of the debtor who engages in fraud; rather, such damages are "awarded as an example to others or as a penalty or by way of punishment" and "are not a debt for fraud . . . ." *In re McDonald*, 73 B.R. at 882.

Thus, the language of the statute suggests that the subsection limits nondischargeability to the amount of benefit to the debtor or loss to the creditor the act of fraud itself created. Section 523(a)(2) does not preclude discharge of punitive damages.

II. The Structure of Section 523

An examination of the structure of section 523 also suggests that section 523(a)(2)(A) does not bar discharge of punitive damages.

In ruling on Palmer's appeal, the BAP stated that it was bound by its earlier decision in *Ellwanger*. There, the BAP relied on a footnote to the Supreme Court case of *Kelly v. Robinson*. In *Kelly*, the Supreme Court considered the scope

[2]Where the section now excepts from discharge "money, property [and] services . . . *to the extent obtained by* false pretenses . . .," it previously excepted a debt "for obtaining money, property [and] services . . . by false pretenses. . . ." 11 U.S.C. § 523(a)(2)(A).

of section 523(a)(7), which excepts from discharge a debt "to the extent such debt is a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss." 11 U.S.C. § 523(a)(7). It held that restitution obligations imposed in state criminal proceedings are not dischargeable. In a footnote to *Kelly*, the Supreme Court noted that, "It seems likely that the limitation of § 523(a)(7) to fines assessed 'for the benefit of a governmental unit' was intended to prevent application of that subsection to wholly private penalties such as punitive damages." *Kelly v. Robinson*, 479 U.S. 36, 51 n. 13 (1986). Interpreting this footnote, the *Ellwanger* court concluded, "The language of § 523(a)(2) and § 523(a)(7) when read in harmony compels the conclusion that Congress intended noncompensatory damages to be excepted from discharge only where they are owed to a governmental entity." *Ellwanger*, 105 B.R. at 556.

[3] While we agree with *Ellwanger*'s holding that section 523(a)(2)(A) does not except punitive damages from discharge, we find that this conclusion is overbroad. Even if private creditors cannot avail themselves of section 523(a)(7), they can still rely on other subsections of section 523. *See Placer v. Dahlstrom* (*In re Dahlstrom*), 129 B.R. 240, 246 (Bankr. D. Utah 1991) ("There is nothing in the language of § 523(a) or its legislative history to indicate that subsection (a)(7) was intended to preclude private entities from pursuing nondischargeability judgments of punitive damages under other subsections"). Moreover, *Ellwanger*'s suggestion that *no* subsection of section 523 bars the discharge of punitive damages conflicts with the Ninth Circuit's holding in *Adams* that punitive damages are excepted from discharge under section 523(a)(6). *See Lock v. Scheuer* (*In re Scheuer*), 125 B.R. 584, 593 (Bankr. C.D.Cal. 1991) (discussing *Adams* and *Ellwanger*).

The footnote to a more recent Supreme Court case suggests a reading of section 523 that does distinguish among its subsections. In *Grogan v. Garner*, 111 S. Ct. 654, 659 (1991), the

Supreme Court held that facts in support of the section 523 exceptions need only be proven by a preponderence of the evidence. In a footnote, the Court stated that it did not consider "the question whether § 523(a)(2)(A) excepts from discharge that part of a judgment in excess of the actual value of money or property received by a debtor by virtue of fraud." It noted, however, "[a]rguably, fraud judgments in cases in which the defendant did not obtain money, property, or services from the plaintiffs and those judgments that include punitive damages awards are more appropriately governed by § 523(a)(6)." *Grogan v. Garner*, 111 S. Ct. at 657, n. 2 (citations omitted). The Court cited to a footnote in *In re Rubin* in which the Ninth Circuit observed that:

> [t]he paradigmatic case for § 523(a)(2)(A) seems to arise when a debtor lies to a creditor to obtain a loan and the creditor seeks repayment of the loan in bankruptcy. The paradigmatic case for § 523(a)(6), by contrast, seems to arise when a debtor intentionally injures a creditor and the creditor seeks to make nondischargeable a judgment that he has won in a state court tort action.

Rubin v. West (*In re Rubin*), 875 F.2d 755, 758 n. 1 (9th Cir. 1989) (citations omitted).

The *Grogan* and *Rubin* footnotes reinforce the notion that distinctions should be made among the subsections of section 523. In the regime they suggest, a creditor should seek nondischargeability of a debt for fraud alone under section 523(a)(2). However, where the debtor inflicted "willful or malicious injury," such that punitive damages were awarded, the creditor should seek nondischargeability under 523(a)(6). For punitive damages, then, the appropriate exception to discharge is 523(a)(6); they are not covered by 523(a)(2).

[4] Thus, *Grogan* and *Rubin*, read together with the statutory language, suggest that there are distinctions among the

subsections of section 523, and that section 523(a)(2) does not provide a bar to discharge of punitive damages.[3]

The BAP's holding that section 523(a)(2) did not except from discharge the punitive damages portion of Palmer's judgment against Levy is therefore AFFIRMED.

[3]Because the BAP relied heavily on *Ellwanger* in its decision on his case, Palmer attempts to distinguish that decision. Our holding does not adopt in full *Ellwanger*'s reasoning nor does it depend on the facts of that case; thus, we need not address his arguments on this point. We note, however, that they do not succeed. While *Ellwanger* involved a statutory penalty rather than punitive damages, its holding was not limited to that context. Palmer argues that punitive damages, in contrast to statutory penalties, bear some relationship to the aggrieved party's loss or the wrongdoer's gain. However, this does not appear to be a traditional requirement of the common law. *See Pacific Mut. Life Ins. Co. v. Haslip*, 111 S. Ct. 1032, 1042 (1991) (punitive damages "hav[e] in view the enormity of [the defendant's] offence rather than the measure of compensation to the plaintiff") (citing *Day v. Woodworth*, 13 How. 363, 14 L.Ed. 181 (1852)). Moreover, there is no indication such a relationship existed between the actual and punitive damages awarded in Palmer's case against Levy. Palmer also argues that punitive damages may be compensatory in nature, and may be awarded when it is too difficult to determine the extent of the plaintiff's actual loss. However, as the BAP notes, there is no evidence that punitive damages served such a compensatory function in this case.

APPENDIX B

APPENDIX B

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

BAP No. CC-87-1142 MeVMo

Bk. No. LA 85-19207 WL

In re TED R. LEVY,

Debtor.

WILSON S. PALMER,

Appellant,

v.

TED R. LEVY,

Appellee.

Argued and Submitted July 20, 1988

at Pasadena, California

Submission Vacated September 2, 1988

Resubmitted on December 13, 1989

Filed: May 25, 1990

Appeal from

the United States Bankruptcy Court
for the Central District of California
Honorable William Lasarow,
Chief Bankruptcy Judge, Presiding

Before: Meyers, Volinn and Mooreman,
Bankruptcy Judges

I.

A judgment creditor sought to have the Bankruptcy Court declare his compensatory and punitive damages nondischargeable pursuant to Section 523(a) of the Bankruptcy Code ("Code"). Plaintiff appeals from that portion of the judgment holding that the punitive damages were not excepted from the discharge. We AFFIRM.

II

FACTS

The Appellee-debtor Ted R. Levy was one of the principals of three real

estate development corporations. These companies hired the Appellant Wilson S. Palmer as a salesperson, promising to pay him commissions and a percentage of profits. Palmer's contract was breached by his employers, causing Palmer to sue Levy and the others in California state court for fraud and misrepresentation. The jury awarded Palmer $45,612.39 in compensatory damages, plus $250,000 in punitive damages. Levy appealed and while the appeal was pending he filed a petition under Chapter 7 of the Code.

Palmer then filed a Complaint with the bankruptcy court to declare both the compensatory and punitive damages to be non-dischargeable under "11 U.S.C. Section 523(a)(2)(6)" [sic]. At the hearing, the entire state court transcript of the fraud trial was offered into evidence. The trial court

found as a fact that the state court "judgment represents a debt which is non-dischargeable pursuant to 11 U.S.C. Section 523(a)(2)." As conclusions of law, the trial court determined that the sum of $45,612.39 was nondischargeable as the result of fraud and false pretenses; but that, exercising discretion, Levy was discharged from responsibility to pay the $250,000 punitive damages portion of the judgment.

III

STANDARD OF REVIEW

This Panel reviews questions of law de novo and findings of fact according to the clearly erroneous standard. In re Rubin, 875 F.2d 755, 758 (9th Cir. 1989); In re Wood, 96 B.R. 993, 995 (9th Cir. BAP 1989); In re Greene, 96 B.R. 279, 282 (9th Cir. BAP 1989). Since no

facts are disputed, the review of this case is de novo.

IV

DISCUSSION

This appeal presents the single issue of whether debts are excepted from discharge under Section 523(a)(2) of the Code where such debts represent the punitive damages assessed against a debtor for false pretenses, false representation, actual fraud or use of materially false written statements. Cases hold that punitive damages are nondischargeable when stemming from similar activities under Section 523(a)(4) (prohibiting "fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny") and Section 523(a)(6) (prohibiting "willful and malicious injury by the debtor to another entity or to the property of

another entity"). However, a distinction is drawn in the Ninth Circuit and elsewhere for cases arising from Section 523(a)(2). We therefore uphold the result reached by the trial court to discharge Levy's punitive damages debt.

A. Case Authority Distinctions Between Sections 523(a)(4),(6) and 523(a)(2)

The case of In re Adams, 761 F.2d 1422 (9th Cir. 1985) illustrates a line of cases arising under Sections 523(a)(4) and (a)(6) in which punitive damages are held to nondischargeable. Robert Adams, the debtor, was found liable for injuries to Betty Moraes in an automobile accident stemming from Adam's intoxication. The entire liability, comprised of $258,000 for general damages and $75,000 in punitive damages,

was held by the trial court to be nondischargeable in bankruptcy under Section 523(a)(6).

On appeal, Adams argued that both compensatory and punitive damages should be dischargeable. In affirming nondischargeability for both aspects of the debt, the Ninth Circuit stated:

> The exception [to discharge] is measured by the nature of the act, i.e., whether it was one which caused willful and malicious injuries. All liabilities resulting therefrom are nondischargeable. . . . Both types of liability are within the statute as "liabilities for "willful or malicious injuries to the person or property of another."

761 F.2d at 1428 (emphasis in original). Accord, In re Austin, 93 B.R. 723, 729 (Colo. 1988). But compare In re McDonald, 73 B.R. 877, 882 (N.Tex. 1987) (holding punitive damages dischargeable under both Section 523(a)(2) and (a)(6)). Punitive damages have similarly been held nondischargeable in cases arising out of Section 523(a)(4), which excepts from discharge those debts incurred by fraud or defalcation while acting as a fiduciary, embezzlement, or larceny [sic]. See, e.g., In re Gelman, 47 B.R. 735, 738 (S.Fla. 1985). See also In re Wallace, 840 F.2d 762, 765-66 (10th Cir. 1988).

In cases governed by Section 523(a)(2) an alternate view is more common: that punitive damages are dischargeable. See, e.g., In re Ellwanger, 105 B.R. 551, 555 (9th Cir. BAP 1989); Matter of

Larson, 79 B.R. 462, 465 (W.Mo. 1987); Matter of Church, 69 B.R. 425, 434-35 (N.Tex. 1987); Matter of Suter, 59 B.R. 944, 946-47 (N. Ill. 1986). See also In re Brown, 66 B.R. 13, 16 (Utah 1986). The distinction drawn is based in the specific statutory language. Section 523(a)(2) reads in pertinent part:

> (a) A discharge under . . . this title does not discharge an individual debtor from any debt--
>
> (2) for money, property, services, . . . to the extent **obtained by -**
>
> (A) false pretenses, a false representation, or actual fraud . . .
>
> (B) use of a statement in writing -
>
> (i) that is materially false
>
> (ii) respecting the debtor's

> . . . financial condition;
> (iii) on which the creditor
> . . . relied; and
> (iv) that the debtor caused
> to be made or published with
> to deceive . . . . [emphasis
> added].

According to the interpretation of this language made by In re Ellwanger, supra, 105 B.R. 551, and similar cases, the nondischargeable debt is of money, property or services obtained by the debtor through false pretenses, false representation or actual fraud. Actual damages represent the loss to the claimants or the increase in the debtor's estate due to false pretenses or fraud. In contrast, punitive damages are said not to represent assets wrongly obtained by the debtor. Rather, such damages are "awarded as an example to

others or as a penalty or by way of punishment. . . . [T]he punitive damages awarded are not a debt for fraud or for a willful and malicious injury." In re McDonald, supra, 73 B.R. at 882. Since the instant case arises under Section 523(a)(2), we are bound to follow Ellwanger unless the Appellant is able to distinguish himself from its holding.

B. The Ellwanger Decision

The submission in the instant case was vacated to await the Ellwanger decision. After Ellwanger was filed, the Panel called for supplemental briefing by Palmer and Levy. The Appellant responded with an attempt to limit the application of Ellwanger by restricting it to its facts.

Palmer contends that Ellwanger holds only a private statutory penalty can be discharged under Section 523(a)(2).

Palmer further argues that private statutory penalties are historically and functionally different from punitive damages. Therefore, maintains the Appellant, Ellwanger does not require the result that punitive damages are dischargeable under Section 523(a)(2). We disagree for three reasons.

First, Ellwanger itself does not distinguish between private statutory penalties and punitive damages. In fact, Ellwanger consistently uses the general phrase "noncompensatory damages" to describe the non-actual damages that may be discharged.

Second, Appellant claims that punitive damages differ from private statutory penalties in that punitive damages must bear some reasonable relationship to actual damages. Such a claim is empirically questionable. Even if it

were true, however, such a relationship between actual damages and punitive damages does not undermine the fundamental premise underlying this aspect of Ellwanger: namely, that actual damages require debtors to disgorge the increases of money or property that were obtained by false pretenses or fraud, whereas noncompensatory damages are awarded without regard to any such increases in debtor wealth. 105 B.R. at 555. Punitive damages and statutory penalties are indistinguishable on this dimension.

The Appellant finally claims that unlike statutory penalties, punitive damages are sometimes functionally equivalent to actual damages and used in lieu thereof. No facts in the instant case, however, suggest that the punitive damages served any such purpose.

V

CONCLUSION

However appropriate it may be in cases arising under Sections 523(a)(4) or 523(a)(6) to treat actual damages and punitive damages alike for discharge purposes, explicit case authority from this Circuit requires a different treatment for debts arising under Section 523(a)(2). Punitive damages are not excepted from the discharge even where the actual damages stemming from the same actions of the debtor may be so excepted.

The trial court deemed the dischargeability of punitive damages under Section 523(a)(2) to be a matter of judicial discretion. As explained above, punitive damages simply do not qualify for nondischargeability under Ellwanger. The Panel may affirm,

however, on any ground found in the Record. Lee v. United States, 809 F.2d 1406, 1408 (9th Cir. 1987); City of Law Vegas, Nev. v. Clark County, Nev., 755 F.2d 697, 701 (9th Cir. 1985); In re Curry and Sorensen, Inc., 57 B.R. 824, 829 n.5 (9th Cir. BAP 1986).

AFFIRMED.

APPENDIX C

APPENDIX C

UNITED STATES BANKRUPTCY COURT

CENTRAL DISTRICT OF CALIFORNIA

Bk. No. LA 85-19207 WL

Adv. No. 86-0246 WL

Chapter 7

In re TED R. LEVY,

Debtor.

WILSON S. PALMER,

Plaintiff,

vs.

TED R. LEVY,

Defendant.

JUDGMENT FOR NON-DISCHARGEABLE DEBT

[Filed January 23, 1987]

Date : January 5, 1987

Time : 8:00 a.m.

Place: Courtroom "H"

This matter having come on hearing on January 5, 1987, at 8:00 a.m., before the Honorable William Lasarow, Bankruptcy Judge presiding in Courtroom "H", in the 9th Floor, United States Courthouse, 312 North Spring Street, Los Angeles, California, upon the Complaint to Determine Debt to be Non-Dischargeable, filed by Wilson S. Palmer, the Plaintiff herein, and Plaintiff having appeared through his counsel, Richard M. Moneymaker, of the Law Firm of Moneymaker & Kelley, and Ted R. Levy, the Defendant having appeared through his counsel Don H. Teague, and based upon the Court's Findings of Fact and Conclusions of Law,

IT IS HEREBY ORDERED, ADJUDGED AND

DECREED that Wilson S. Palmer has a non-dischargeable debt against Ted R. Levy in the sum of $45,621.32 [sic] plus costs in the sum of $2,637.15

Dated: 23/JAN/1987

/s/ William J. Lasarow

WILLIAM J. LASAROW

UNITED STATES BANKRUPTCY JUDGE

APPENDIX D

UNITED STATES BANKRUPTCY COURT

CENTRAL DISTRICT OF CALIFORNIA

Bk. No. LA 85-19207 WL

Adv. No. 86-0246 WL

Chapter 7

In re TED R. LEVY,

Debtor.

WILSON S. PALMER,

Plaintiff,

vs.

TED R. LEVY,

Defendant.

FINDINGS OF FACT AND CONCLUSIONS OF LAW RE: JUDGMENT DECLARING DEBT NON-DISCHARGEABLE

[Filed January 23, 1987]

Date : January 5, 1987

Time : 8:00 a.m.

Place: Courtroom "H"

This matter having come on hearing on January 5, 1987, at 8:00 a.m., before the Honorable William Lasarow, Bankruptcy Judge, in Courtroom "H", in the 9th Floor, United States Courthouse, 312 North Spring Street, Los Angeles, California 90012, upon the Complaint to Determine Debt to be Non-Dischargeable, filed by Wilson S. Palmer, the Plaintiff herein, and the Plaintiff having appeared through his counsel, Richard M. Moneymaker, of the law firm of Moneymaker & Kelley, and Ted R. Levy, the Defendant having appeared through his counsel Don H. Teague, and evidence both orally and documentary having been presented to the Court and good cause appearing therefor,

The Court now finds and concludes as follows:

FINDINGS OF FACTS

1. That on or about March 7, 1986, Los Angeles Superior Court Judge George G. Grover, Jr., entered a Judgment in the Superior Court of Riverside County, Case No. 14585, in favor of Wilson S. Palmer ("Palmer") and against Ted R. Levy ("Levy") among other Defendants for compensatory damages in the sum of $45,612.39 and punitive damages in the sum of $250,000.

2. That said Judgment was obtained after a jury trial lasting approximately 9 days, in which 6 witnesses were called to testify.

3. That Levy thereupon filed a voluntary petition in Bankruptcy in the Bankruptcy Court, December 30, 1985, and scheduled as a creditor, Palmer and

listed as an obligation the amount of said judgment.

4. That subsequently Palmer filed this Complaint against Levy to Determine the Debt to be Non-Dischargeable, contending that said Judgment obtained in Los Angeles Superior Court constituted a Non-Dischargeable Judgment pursuant to 11 U.S.C. Section 523(a)(2)(6).

5. That Levy filed an Answer to said Complaint, and the matter was set for trial.

6. That at the trial the entire Reporter's Transcript of the Superior Court Jury Trial, was offered as an Exhibit and pertinent parts of it were read into evidence and testimony was given by John Hoover, counsel for Palmer, who conducted the State Court jury trial on Wilson Palmer's behalf.

7. That Levy was called as a witness and also testified.

8. The Court refused to allow Levy to challenge the amount of said judgment, but did allow testimony as to the nature of the debt in judgment obtained by Palmer.

9. That this Court finds that the Superior Court jury were given BAJI instructions, which establish an identical legal standard for fraud and misrepresentation, as that found in 11 U.S.C. Section 523(a)(2). That this Court finds that there is sufficient evidence in the record to support a judgment for fraud by the Superior Court jury.

10. That this Court finds that the judgment represents a debt which is non-dischargeable pursuant to 11 U.S.C. Section 523(a)(2).

CONCLUSIONS OF LAW

1. This Court concludes that the Superior Court Judgment obtained March 7, 1985, by Palmer v. Levy is res adjudicata as to the amount of said judgment, in the sum of $45,612.39.

2. This Court concludes that the record of the State Court Judgment is evidence that Levy is liable to Palmer on a non-dischargeable debt in the sum of $45,612.39, for fraud and false pretenses arising out of the underlying facts and transactions, which were presented to the jury in the State Court action.

3. This Court concludes that it has discretion, however, to discharge Levy from legal responsibility to paying the $250,000 punitive damage portion of the

judgment.

Dated: 23/JAN/1987

/s/ William J. Lasarow

WILLIAM J. LASAROW

UNITED STATES BANKRUPTCY JUDGE